



## SIXTY YEARS AFTER THE UN PARTITION RESOLUTION: WHAT FUTURE FOR THE ARAB ECONOMY IN ISRAEL?

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*Despite the expectations of economic theory, a century of Arab-Jewish economic interaction in Palestine has not led to the convergence that is supposed to result from exchange between a capital-rich economy and a labor-intensive one. After 60 years of failed integration, the Arab population in Israel has fallen to the bottom of the socioeconomic ladder. With the Palestinian “regional economies” in Israel and the occupied territories operating as part of the same Israeli economic regime, the challenge for Palestinian economic policy makers is to build on the new paradigm in shaping a national development strategy aimed at reconstructing Arab-Jewish economic relations on the principles of balanced cooperation embodied in the Economic Annex of the 1947 UN partition resolution.*

SIXTY YEARS AFTER the establishment of the State of Israel, the Palestinian Arab people who remained behind and were incorporated as a minority within the state face an uncertain future. Abandoned politically by the Palestinian national movement and its authority in the occupied territories, they remain on the margins of Israeli politics, society, and culture. Nevertheless, these “Arab Israelis”<sup>1</sup> have important lessons to impart to their Palestinian compatriots, especially in terms of steadfastness in the face of adversity. A determining factor in their survival as a national (not an ethnic) minority has been the manner in which the limited economic resources and assets at their disposal have been identified with their nationality, or their “Arabness,” in a Jewish state. In a similar way, Israeli settlement and separation policies in the occupied territories have consolidated a Palestinian economic entity that has been the backbone of the survival of a fledgling national identity and entity. As the viability of the two-state vision appears to recede with time, the challenge of envisioning the economic underpinnings of an eventual one-state resolution of this century-old conflict grows.

This essay is premised on the observation that the economy of the Arab region in Israel<sup>2</sup> and the Palestinian economy in the occupied territories, today

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both operating within the Israeli economic system, constitute the remnants of the Arab part of the dual economy that functioned in Mandatory Palestine until 1948. A brief review of the various theses and counter-theses advanced in socioeconomic research on the Palestinians in Israel demonstrates how Israeli political economy explanations for the Arab-Jewish development gap were eventually countered and effectively outflanked by a body of mainly indigenous Palestinian Arab narratives. Available data on the macro and sectoral levels help draw an up-to-date picture of the de-developed socioeconomic status of Palestinian Arabs in Israel. Without making the links explicit here, this review implies a range of possible outcomes for the Palestinian economy in the West Bank and Gaza Strip (WBGS) under prolonged occupation. This macroview of the Palestinian Arab economies operating today within the Israeli economic orbit forms the starting point for suggesting that the time is opportune for a new vision of a Palestinian national economic strategy that deploys a range of subregional economic assets and coordinated development programs.

### **THE DUAL ECONOMY: FROM PARTITION 1947 TO RE-PARTITION 2007**

One of the ironies of the history of the Palestine question is that while the two-state territorial partition solution of UN General Assembly (UNGA) Resolution 181 of 1947 remains elusive, its economic annex, which transformed the dual-economy model of Arab-Jewish relations in Palestine into a plan for “economic union,” has been realized and has been operational on a *de facto* basis since 1967. With the Israeli fiscal, monetary, and trade regime in force throughout Israel and the occupied territories, economic union in its most advanced form (albeit of the lopsided dual-economy variety) is the economic law of the land. Needless to say, this has emerged along different boundaries and on principles contrary to those envisioned by the framers of UNGA Res. 181.

As the British Mandate in Palestine drew to a close in 1947, a dual economy model of Jewish-Arab economic relations had already started to take shape, diffused territorially and demographically throughout the country. However unbalanced, unequal, and separate the Arab and Jewish economic sectors may have been, they were nonetheless linked, and together they constituted the “national” economy of Mandatory Palestine.<sup>3</sup> Despite a demographic balance overwhelmingly in favor (2:1) of the Palestinian Arab population, the economy of the Jewish minority was predominant, enjoying dynamic links with European capital, industrial know-how, and high-quality human resources. The mainly rural/agrarian Arab economy, by contrast, was clearly at a different stage on the developmental ladder and on a separate trajectory with respect to external trade networks, financial links, and structural transformation processes.<sup>4</sup> Still, exchanges (of labor, merchandise, and services) between the two were intense and often complementary. In this sense, the potential benefits to both sectors of continuing close interaction could be expected, assuming a post-Mandate Palestine in the context of mutually agreed-upon and balanced economic regulations, institutions, and mechanisms.

From the standpoint of the UN's technical experts, who drew up the economic union plan relying on the conventional economic theory and experience of the time, the only option for a future two-state solution was the dual-economy model already emerging between the two communities.<sup>5</sup> It was entirely reasonable to assume that if economic union had been pursued as designed in the context of implementing the political and territorial solution of UNGA Res. 181, such an arrangement should have been able, over time, to achieve the goal of closing the dual-economy gaps of Mandate Palestine. Certainly there was a reasonable possibility in such conditions that a mutually beneficial economic union between two sovereign states might ultimately have been realized through the eventual convergence of per capita Arab and Jewish incomes.

While an effective "economic union" between Israelis and Palestinians did in fact emerge within Israel after 1948, it was not built upon peace, as UNGA Res. 181 had intended it to be. Instead, it was born of intergenerational conflict, military rule, discrimination, occupation, and segregation between an industrializing, advanced, and sovereign center on the one hand and a rural, poor, and leaderless periphery on the other. This has created a re-partition of economic power on the ground today that does not follow the borders or balances assumed in UNGA Res. 181 and which is best understood as an *outcome* of prolonged conflict, if not a tool of domination, as some Israeli strategists have envisioned. What has happened, then, is the opposite of the UN vision of economic union (and, much later, of the Oslo concept of economic cooperation), which was meant to facilitate a *resolution* to the conflict. Without doubt, the economic "union" between Israelis and Palestinians that has emerged is a construct that could not have been envisaged even by the most prescient UN bureaucrats sixty years ago.

In a sense, the dual economy, in its current distorted and unbalanced form, comprises not two distinct economic systems but four. The Jewish Israeli part of the dual economy equation has expanded territorially from within the 1949 armistice lines to encompass and integrate Israeli settlements throughout the West Bank and is ever predominant. The other party to this peculiar dualism, the marginalized and impoverished Palestinian Arab economy, now comprises three separate and distinct economies, each of which is more dependent on the Israeli center than on each other: the remaining noncolonized areas of the West Bank, the now wholly isolated Gaza Strip, and the Arab-majority subdistricts of central and especially northern Israel. After forty years of occupation of the former two regions and sixty years of failed integration of the latter, the economic landscape of the Israeli-Palestinian conflict is now fractured and distorted, the Palestinian economies separated from each other and from the Israeli economy as never before.

As has always been the case, the path of Palestinian economic development remains subordinated to political imperatives and facts on the ground. The forthcoming phase of the prolonged struggle over land, people, and resources in Palestine/Israel will thus retain an important economic dimension.

However, the concept of Israeli-Palestinian economic relations that has been defined by (and prevailed since) the Oslo accords appears increasingly obsolete in light of the political prospects being shaped by the ongoing conflict.<sup>6</sup> Economic policy analysts must therefore recognize the extent to which political and demographic realities on the ground have resulted in an economic power structure that transcends the usual parameters defining the economic implications of a two-state solution.

### CHALLENGES OF PALESTINIAN ECONOMIC DEVELOPMENT IN ISRAEL SINCE 1948

One of the factors generally discounted by politicians, academics, and other observers is the place of Israel's Palestinian minority in the overall Palestinian-Arab/Jewish-Israeli equation. The status of the Palestinians of Israel has at best been considered a marginal political or civil rights issue in domestic Israeli politics—one that cannot even be broached in “final status” discussions. Only since the 1990s have Arab civil society representatives in Israel redefined their relationship to the state: Increasingly, they see it in terms of a struggle for national and cultural autonomy within an Israeli “state of all its citizens,” even as the Arab demographic “threat” continues to feature prominently in Israeli political and academic discourse. Meanwhile, this sixth of Israel's population<sup>7</sup> straddles a geostrategic position in the overall competition for natural resources and national income both within Israel proper and between the Green Line and the current frontiers of Israel's effective control in the occupied territories. This has implications beyond the traditional discussion about the Palestinian-Israeli economic relationship. Whether from the perspective of the Palestinian development research *problematique* or of economic policy-making, these geo/demographic realities take us back to the economic contours and balances envisioned by UNGA Res. 181 as part of any serious discussion of future directions.

Notwithstanding decades of research on many aspects of the Arab economy in Israel, the extensive findings by sociologists, geographers, political scientists, and economists generally show the use of conceptual frameworks and methodological tools that are inappropriate for examining past performance and future prospects. Certainly, scholars working on this issue since the 1960s have made valuable contributions in interrelated areas of research, such as agricultural modernization and land use, labor force dynamics and human resources, class and social differentiation, and entrepreneurial development. However, the economic status and potential of over a million Arab citizens of Israel remains a marginal issue in academic research and in the policy debate surrounding the Israeli-Palestinian conflict. The Arab minority is seen either as an exotic nonissue, a subject for anthropological research, or a worthy cause in the struggle for equality, civil rights, and integration within Israel.

As for the Palestinian minority itself, its still-separate identity, confirmed by stubborn spatial, cultural, demographic, and policy-related realities, has led

to growing calls for political autonomy in Israel, most recently in the various manifestos and “vision papers” of 2006–2007.<sup>8</sup> But the economic implications of a struggle for such a status remain unexplored, whether in the current context of continued absolute Israeli control or in a hypothetical two-state (or even one-state) political solution. The vital economic policy issues on the agenda of the Palestinian minority—especially unemployment, local finances, housing, land tenure, industrial zoning, agricultural viability, poverty, social fragmentation, and delinquency—have yet to be formulated politically into a coherent analysis of the Palestinian development experience in Israel, or

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into a platform with strategic implications. Indeed, the concept of an “Arab economy” in Israel is neither clearly defined nor well-understood, much less accepted. This is mainly because the Israeli democratic state-building narrative has always insisted on presenting the Arab minority as part and parcel of Israeli society and state, as an element of Israel’s self-portrayed “cultural mosaic.” Accordingly, for purposes of academic analysis, the subject has remained at the disaggregated level of Arab workers, farmers, workshops, entrepreneurs, and localities in the Israeli economy.

An important underlying factor that has perpetuated neglect of this issue in the policy analysis of Palestinian development relates to the manner in which it has been treated in most of the literature: that is, as a subtheme of an *Israeli* development experience rather than as a feature of the broader conflict. Much of this literature, dominated by Israeli academics, is devoted to trying to reconcile the subordinate status of Palestinian Arabs in Israel with an assumption of their inevitable eventual “integration” as equal citizens into the Israeli state and hence their access to equal opportunities in the national economy. The methodological acrobatics required to sustain such a suspension of belief are impressive. To explain persistent Arab-Jewish economic inequality in Israel, a range of socioeconomic factors have been cited, including the flight of Palestinian urban elites in 1948; resistance of the Palestinian fellahin to Israeli modernization; the market forces that pulled Israel into the liberalized global economy and left behind “stragglers”; and (in more recent studies) the linkage between the Palestinian minority’s perpetually low occupational status and educational achievements. Cause and effect are often reversed in the quest for an economic narrative that fits with Israel’s democratic credentials so as to buttress the notion of equal rights and opportunities for all citizens.

Research and academic literature on Palestinian economic conditions in Israel can conveniently be classified under two broad categories largely defined by the explicit or implicit ideological positions they embody. The oldest and most pervasive trend, which emerged in the 1960s from the liberal, social-democratic tradition of Israeli academia, has today evolved into a form of “Zionist neoliberalism.”<sup>9</sup> Emanating from a humanist reaction to the devastation wrought by Zionism against the Palestinian inhabitants of the country, this

school of thought has always reflected a blind faith in the justice of the Israeli system, an assumption of equal rights for non-Jews in a Jewish state, and a die-hard belief that the operation of the market and the occasional state-sponsored policy palliative could somehow correct the numerous distortions created by nonmarket forces.

The subtext of much of the research under this category reflects both the “security first” logic of Arab development in Israel and the deep-rooted Zionist fears of the Arab demographic threat. This body of research, which has flourished since the 1980s as the state grappled with rising Palestinian-Arab nationalist mobilization in Israel, has sustained the lingering belief that growing gaps and distortions are amenable to correction by market forces (or, if need be, by programmed government intervention and positive discrimination). Even recently, a group of highly respected Israeli economists proposed to revisit the question of “whether Israeli Arabs operate in the same markets as the rest of the population” and whether “two distinct ethnic markets” exhibit “convergence over time”<sup>10</sup>—as if this were a question that required yet more academic inquiry.

The second broad category, best grouped under the rubric of “non-Zionist political economy,” developed later, especially since the 1980s, as new insights into the socioeconomic situation of Palestinians in Israel began to emerge from a number of diverse ideological sources and disciplines. These latter contributions share an understanding of (a) how the Jewish state-building policy environment before and after 1948 resulted in built-in impediments to Palestinian-Arab integration (politically, economically, and socially) within Israel; (b) how successive Israeli governments have failed to address (much less act to ameliorate) the core issues; and (c) how historical processes of dispossession, segregation, and marginalization have disempowered the Palestinian minority and created visible ceilings to advancement. Some of this research has come from outside the economic sciences, opening new perspectives on both specific and more overarching aspects of Arab socioeconomic status in Israel. This body of research, like that of the Zionist neoliberal writers, was empirically based and scientifically rigorous.<sup>11</sup>

The various gaps and constraints noted by writers within the “non-Zionist” group of political economists are understood as part of a comprehensive whole that pits a discriminatory, hegemonic Jewish state (and economy) against an ethno-national minority unable to access its fair share of national resources. The losing struggle to maintain access to natural resources and to obtain national finance for development plays out in persistent gaps and imbalances in Arab educational advancement, occupational progress, and capital accumulation. It also entails an overall deterioration of terms of trade (labor, goods, and services) between the Arab (“regional”) economy and the Jewish (“national”) economy.<sup>12</sup>

Notwithstanding the different disciplines and divergent approaches informing the research of the two groups, they do share some consensus on certain points:

- There are persistent gaps between the Arab and Jewish sectors of the Israeli economy in most, if not all, socioeconomic and development indicators.
- These gaps are not coincidences of history, explained simply by comparative sectoral resource allocations; rather, they emanate from distinct external processes that impede the free operation of theoretically perfect (but actually imperfect) markets.
- Although economic convergence in the long term is promised, achieving this is no less complex or certain than is global convergence between developed and developing countries, and it requires sustained policy intervention to assure such an outcome.
- The marginalization of Arabs in Israel is not unrelated to the state's Jewish character and its Zionist development policy preferences and priorities.
- The political, economic, and social processes that have contributed to marginalization of the Arab economy began well before 1948 and continue today to lock in and further degrade the position of Arabs in Israeli economy and society.<sup>13</sup>

On the other hand, clear differences of opinion remain on some major points:

- Whether the determinant processes that have perpetuated Arab underdevelopment in Israel are related primarily to internal (Arab) constraints and the "normal" development path, or whether they are intrinsic to the particular (existential) situation of being *Palestinian Arab* in a *Jewish state*;
- Whether the overall impact of the modern, capitalized, liberalized, and globally connected Israeli Jewish economy has been to pull the rural, less-developed, traditional Arab society into the twenty-first century, or whether its impact has been to maintain the Arab sector's less-developed, subservient, and fragmented status and its role as a source of cheap labor, goods, and services, and as a captive consumer market;
- Whether the Palestinian minority will remain leaderless, lacking the necessary "self-consciousness" and distinct, separate identity within Israel, or whether it will succeed in mobilizing itself and its full weight within the Israeli-Palestinian-Arab conflict.

What seems beyond question is that without a radical rethinking and political repositioning of the Arab minority in Israeli politics and society, as well as within the broader context of the Israeli-Palestinian context, effective policies and programs that favor the development of the Arab economy in Israel are unlikely to emerge.

#### **THE PERSISTENCE OF AN ARAB "REGIONAL" ECONOMY IN ISRAEL**

In 1988, I published the findings of my own examination of the Arab economy in Israel that utilized tools of (subnational) regional economic analysis.<sup>14</sup>

The analysis identified four factors that defined and delineated the Arab “region”: (1) Israeli state policy; (2) geophysical features; (3) the Arab community’s social, political, and cultural network and organization; and (4) persistent economic differentials (*vis-à-vis* the Jewish economy). My analysis of the Arab-Israeli economy as a marginalized, impoverished, and largely subservient *region* of a *national* (Jewish/Zionist) economy served the dual objective of elaborating a comprehensive profile of its structure and performance and of providing a policy framework in which a strategy and program for its sustained development could be designed and implemented.

Such a strategy could hardly be expected from the Israeli state and would have been possible only from Palestinian economic/development policymakers willing to take up the challenge of fitting the Arab-Israeli economy within a broader program of civil resistance, development, and institution-building that would also encompass the Palestinians in the occupied territories. In fact, the post-Oslo configuration on the ground could have made such an option more feasible, because *economic* exchanges between Palestinians in Israel and Palestinians in what became the PLO-ruled areas of the WBGS were legitimized and expanded during this period. At the same time, however, the political conditions imposed by the Oslo accords removed Israel’s Palestinian minority from the Palestinian-Israeli negotiating agenda and effectively severed the *political* links that had hitherto developed between the Palestinian civil society and political elites in Israel and the PLO (in exile). While the Palestinians in Israel may have seen themselves as “an inseparable part of the Palestinian people,”<sup>15</sup> the terms of Oslo and the PLO’s preoccupation with the affairs of the new Palestinian Authority (PA) clearly placed them on the Israeli side of the political border, separating them from the arena of the Israeli-Palestinian conflict. From that time forward, their concerns were relegated to the domain of civil and human rights issues, as if their share in final status issues had already been unilaterally resolved as an internal Israeli affair.

Twenty years after my study, it is timely to assess how well the regional economic model of the relationship between the Arab and Jewish sectors in Israel reflects current realities by reviewing key gaps and relationships in light of more recent data. What remains to be seen is whether or not the Arab-Jewish economic imbalance in Israel, if not that between Israel and the occupied territories, is defined by the persistence of economic divergence and its enduring geo/ethnic contours. The potential relevance of such a model as a policy-making tool seems even greater in the light of the latest wave of Palestinian Arab “regional autonomy” activism, especially as persistent socioeconomic gaps can have a social “consciousness-creating” effect over a prolonged period.

Currently available data are not easily comparable with those used in my previous research for regional spatial analysis, so it is not possible here to make direct comparisons with the indicators used for the situation in the mid-1980s. However, new comparative socioeconomic data for Arab and non-Arab localities published by the Israeli Central Bureau of Statistics (ICBS)<sup>16</sup> confirm the extent to which the poorest and weakest sectors of the Israeli economy



are predominantly Arab, as well as the extent to which the Arab economy is predominantly poor. An Israeli version of a “human development index” for 2003 covers 197 Israeli local councils and municipalities, accounting for just under 6 million people. These councils and municipalities include the bulk of the Israeli population (6.4 million in 2003) as well as almost all localities in Israel.<sup>17</sup> Of the total 197 localities covered, 70 are Arab, representing some 838,000 persons, or about 80 percent of the Arabs of Israel. The remaining 250,000 Arab Israelis live in the smallest villages or are included in indicators for the five mixed cities (Acre, Haifa, Ramla, Lod, Jaffa).

The ICBS data on this critical mass of the Arab-Israeli economy paint a dismal picture of the results of sixty years of failed integration (and Arab exclusion) in Israel. Of the 197 Arab, Jewish, and mixed localities, 102 show composite socioeconomic indices below the median. Of these localities, two-thirds (66) are Arab. Only four small Arab villages are above the median. Of the 10 localities at the bottom of the index, seven are Arab; of the 70 least advantaged localities, 52 are Arab. When the unweighted averages (for almost all indicators) are compared, the differences between the Arab population and the national average acquire sharper focus:<sup>18</sup>

- The median age of the Arab population included in the ICBS index is 8 years below the median age of the national population (28 years), implying major long-term employment challenges for a young and growing Arab population;
- While only 16 percent of Israeli families have four or more children, the Arab average is twice as high (33 percent), attesting to increasing pressure on housing, social services, and utilities within the Arab sector;
- Arab average per capita income (at around NIS 1,300 per month, approximately \$300) is under half the national average, though the gap has narrowed over time;
- Whereas 44 percent of the total population were “sub-minimum wage earners,” 57 percent of Arabs fall within that category;
- Conversely, 8.6 percent of all Israeli full-time employees earned more than twice the minimum wage, as compared to about 2 percent of Arabs;
- Educational achievement is the only category where the gap is relatively narrow: 40 percent of Arab students attain their secondary matriculation certificate, compared to a national average of 49 percent;
- By contrast, fewer than 7 percent of Arabs between the ages of 20 and 29 are in higher education, compared to a national average twice that.

This snapshot of socioeconomic gaps is underpinned by many factors, too numerous to present here but well covered in the wealth of non-Zionist literature referred to above. Suffice it to say that one of the most important features in the transformation of the Arab economy in Israel has been agricultural decline and marginalization. It is true that the falling share of agriculture in Israeli GDP reflects a developmental transformation, whereby heavy, medium, light (and

later high-tech) industries and services gradually replaced agriculture as the leading production and export sector. But the contraction in Arab agriculture was not accompanied by the emergence of more productive, technologically advanced industrial activities. Moreover, it must be noted that the contraction in Arab agriculture was primarily a consequence of extensive land expropriations by the state through the 1980s, compounded by pressures on the remaining land by a rapidly growing rural population (leading to a process that has been termed *in situ* urbanization) as well as by competition from a highly organized, state-supported Jewish agricultural export establishment.

The decline in Arab agriculture can be glimpsed through reference to agricultural and crop area changes over the past thirty years. Available data<sup>19</sup> tell us that whereas the total area devoted to agriculture in Israel has actually expanded by 4 percent over that period, in the Arab region it has fallen by 16 percent. As non-crop agricultural activities (livestock, fisheries) have increased their share of total area devoted to agriculture in Israel, the area devoted to crops has fallen by 5 percent; in the Arab economy, the decline in crop area has been 25 percent. In both the national and regional economies, this has been offset by a steady increase in livestock breeding of around 150 percent in the Arab sector and about as much in the Jewish sector. By 2001, more than 50 percent of Israeli livestock was within the Arab sector, indicating a rational shift by Arab farmers into more lucrative sectors of Israeli agriculture.

Meanwhile, the pattern of utilization of crop areas—fruit and olive plantations, vegetables/potatoes/melons (mainly irrigated) and (rain-watered) field crops—has shifted nationally (especially in the Jewish economy) away from the third branch toward cultivation of export/cash crops, especially in the second branch. In Arab agriculture, the decline in field crops was accompanied by a steady decline in the cultivation of more lucrative (and labor-intensive) vegetables. The Arab farmers' move away from this water-intensive branch of agriculture has been rationally motivated, their state-determined water quotas having always been lower than those of Israeli collective farms and kibbutzim. Consistent with the increasingly unattractive long-term income prospects of agriculture in Israel, the struggle over resources, and the increasing pauperization of Arab rural communities, the greatest shift in Arab agriculture has been the steady increase (67 percent over 30 years) of land devoted to (mainly olive) plantations, which constitute around 25 percent of all Israeli plantations. Of the 179,000 dunams<sup>20</sup> of Arab olive and fruit plantations in 1999, 22 percent were irrigated; of the much larger area of 849,000 dunams of plantations cultivated by Jewish farms, 82 percent were irrigated, seventeen times the Arab irrigated plantation area.<sup>21</sup>

The labor force characteristics of Arabs in Israel also continue to exhibit important differentials vis-à-vis the Jewish labor force, though less sharply than in the past. Whereas labor force participation rates of Arab males are close to those of Jewish males, low Arab female participation keeps the overall average at around 40 percent, compared to a national average of 60 percent.<sup>22</sup>

Unemployment rates among Israeli Arabs are consistently higher than in the Jewish economy (12 percent compared to 8.3 percent in 2000). Arabs are also more concentrated than Jews in low-skilled occupations. The largest two sectoral employers of Arabs in Israel are manufacturing (20.6 percent of all employed) and construction (15 percent), which employ only 17.8 percent and 3.8 percent of Jews, respectively. A larger proportion of the Jewish labor force is employed in public and private services than Arabs: 34 percent and 38 percent, compared to 26 percent and 33 percent, respectively. Meanwhile, agriculture, which employed 17,000 Arabs in 1980, employed only half as many by 2000 (not all of them employed on Arab farms).

One should not conclude from the above outline of Arab-Jewish socioeconomic differentials that time has stood still for Arabs in Israel, or that they have been totally bypassed by Israeli development. Many basic needs, such as health care, universal education, and social welfare, have not been neglected by the state, and proximity to the more advanced Jewish economy has allowed for "gains" that many Palestinians living under occupation or in exile would envy. The newest Arab generation is increasingly "Israelized" (and "globalized") culturally, as the pre-1948 traditions that sustained social cohesion gradually falter (which has resulted in a degradation of social capital). Furthermore, the progressive path of Israeli economic development has freed up middle occupational levels where Palestinians hitherto could not compete. The result is that more educated Arab professionals are gaining a foothold in the national economy outside the specific context of the traditional Arab communities where they were raised.

Such facts should not be discounted in any assessment of how far Palestinian Arabs in Israel have progressed in sixty years, and what potentialities that creates for their future. For example, the emergence of Israeli Arab capitalists, generated largely through services and commerce (as compared to limited industrial capital investment accumulated up to the 1990s) is an indicator of the potential for mobilizing ethnic economic power. Although much is conspicuously consumed by these new Arab commercial elites, or "saved" through residential construction and land acquisition (but rarely invested in new enterprises), a financial policy framework for mobilizing more "developmental" investment within the Arab region remains sorely lacking.

Overall, however, there is little evidence of significantly greater Arab integration in the Israeli economy today than in the past. Economic exchanges between Arabs and Jews in Israel have not entailed inclusive development, and they continue on the distorted and disadvantaged basis that has always characterized the regional-national relationship. However many economic success stories we may hear of Palestinians in Israel, a "regional" approach to understanding the overall economic "de-development" of the Arab sector has not lost its validity. In fact, most of the success stories are uniquely "Arab" insofar as they result from a struggle against adverse conditions and show the entrepreneurial tenacity and social adaptability that can be generated by prolonged and dire hardship.

The structural trends and binding constraints on which Israeli economic success has depended are the very factors that have perpetuated a separate and dependent economic status of a million Palestinian Arabs in Israel. The latter's economic fate is almost as confined to the limited space in which they reside as is the fate of the economy of the Palestinian people encircled in Gaza or fragmented in zones behind the separation barrier. Political developments among the Palestinians in Israel in the wake of the Oslo accords, which have featured growing Arab political autonomy and calls for more, beg an autonomous (read: *regional*) social and economic development strategy powered from within and self-reliant to the extent possible. It is about time that the lessons of Palestinian economic development under prolonged conflict are absorbed and the potential for mobilizing "ethnic economic power" are seriously explored.

### AN ECONOMIC PARADIGM FOR THE ONE-STATE SOLUTION?

Even after seven years of intifada, disintegration, and growing Israeli-Palestinian physical and economic separation, discourse on Israeli-Palestinian economic relations still generally assumes the possibility and desirability of achieving a balance in respective power and interests of two sovereign states. At the least optimistic, there is a supposedly a possibility of levelling the playing field between the two unequal partners through policy interventions, appropriate trade regimes, aid, and cooperation between them. Whereas this may have still seemed plausible as late as 2000, such a starting point quite simply no longer exists. The Israeli-Palestinian customs union established in 1994 remains the *de jure* framework for relations between the West Bank and Israel, but its weaknesses, inherent from the outset, are now fully exposed as Israel applies its provisions selectively and in line with its security and political agendas.<sup>23</sup> Thus, while economic analysts and policymakers question the rationale of prolonging the current dysfunctional framework for Israeli-PA economic relations (not the subject of this essay), it is useful to take a broader view, unencumbered by conventional assumptions about what is desirable and attainable for Palestinian development in the present circumstances.

Of relevance here is a dimension of the Arab-Israeli economic landscape that had growing importance from the 1990s until 2000: the (largely undocumented) economic links between the Arab-Israeli economy and the Palestinian economy in the WBGS under the PA. These links did not reach a degree of economic *integration*, but could be described as intensive and focused *exchange*. The mainly informal commercial, labor, and financial relations that emerged between the Galilee/Triangle areas and the WBGS expanded during the second half of the 1990s, especially as the latter grew during that period. The exchanges were indicative of more than just market forces or even geographic proximity, but they were abruptly constrained as the physical separation between Israel and the WBGS deepened.

For both sides of the exchange, the common basis of the relationship differed from that which exists between (non-Arab) Israeli consumers, contractors, or

exporters and the economy administered by the PA. Common factors such as consumption patterns, income levels, business culture, language, and social solidarity naturally placed the relationship between the Arab-Israeli and PA economies in a different category from that between the Israeli and PA economies. Even today, many Galilee- or Triangle-based Arab capitalists and commercial agents maintain business flows with WBGS markets through the Jerusalem-Ramallah corridor and other limited contact/entry points. Until 2001, Gaza enjoyed a booming export trade with Arab Israelis who came by the busload to buy cheap imported Egyptian consumer goods and fresh Gaza agricultural produce. Throughout the Oslo period, workers from Gaza found regular employment and shelter in Arab communities in northern Israel; today they are hunted down relentlessly by Israeli police as illegal migrants. This distinctive link has been severed, and the Gaza region of the Israeli-Palestinian economic cluster is today totally isolated from both the Palestinian economy in the West Bank and the Arab regional economy further to the north.

Whereas these subregional relationships were very far from approximating a “neo-dual economy” model, the comparative advantages characterizing the exchanges between the WBGS and the Arab regional economy in Israel demonstrate structural complementarities that must be explored. At the current stage of the conflict, as the two-state option seems to recede—to be replaced by unknown outcomes—it appears timely to project what has been learned about historical processes and what we know about the economic facts on the ground with a view toward elaborating a strategic developmental policy framework in line with the emerging realities of the Palestinian-Israeli conflict. Fresh empirical and analytical research (beyond the scope of this article) could demonstrate that the functional relationship linking all components of the Arab *regional* economy (i.e., the Arab economies in the West Bank, Gaza Strip, and the Galilee/Triangle) with the Israeli *national* (i.e., Jewish) economy is one of an isolated, less advanced (or de-developed) *regional* economy (periphery) and an expanding, liberalized, high-tech *national* economy (center).<sup>24</sup>

One of the new realities is that the attributes of institutional, administrative, and limited fiscal autonomy acquired by the economy administered by the Palestinian Authority in 1994 has been largely lost in recent years.<sup>25</sup> Thus, if there is to be a new stage in Palestinian economic governance, it will certainly have to go beyond the experiment that has been the PA. Meanwhile, the still apparently legitimate case for the “viability” of an independent national economy in a WBGS liberated of Israeli settlements and occupation is increasingly rendered redundant by the facts of Israeli colonial expansion. While the separation barrier has cantonized the West Bank, the Israeli “withdrawal/disengagement” from Gaza has transformed realities there into a socioeconomic disaster zone. We appear to be light-years away from the much trumpeted Oslo model of Singapore on the Mediterranean.

Nevertheless, even in the context of Israel’s “separation” policy, the economies of 3.5 million Palestinians in WBGS and another million behind

the Green Line remain fixed within the Israeli economic orbit. The increasingly fragile PA economy remains highly dependent on the center for access to trade, jobs, technology, and consumption of goods and services—even public services such as utilities, health, and education. Both the PA economy and the Arab regional economy in Israel are almost identically affected by national (Israeli) macroeconomic, trade, and most components of fiscal policy.

All these features imply that there is more correlation between the WBGS and Galilee/Triangle than has so far been recognized, whereas the most significant convergence that seems to be occurring is among the impoverished Arab regions themselves. In the last few years the structural resemblances between the Palestinian regional economies have become more striking even as they become more separated physically. Though per capita incomes of Palestinians in the WBGS have plummeted since 2000 to less than half the levels among Arab-Israelis, both regions remain much closer in living standards to each other than to the Jewish economy. While the WBGS economies retain a limited domestic productive base, external trade is conducted entirely with Israel or through Israeli intermediaries. And in all the Palestinian regional economies, domestic capital invested locally finds its safest allocation in real estate. Relatively high educational standards do not translate into better occupational or employment opportunities; unemployment is high in all Palestinian regions. Perhaps the strongest justification for *not* considering Palestinian economic development in Israel/Palestine from the angle of sub-national regional analysis is the political imperative of Palestinian national self-determination within the WBGS territorial boundaries.

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***In the last few years the structural resemblance between the Palestinian regional economies (West Bank, Gaza Strip, and Galilee/Triangle) have become more striking even as they become more separated physically.***

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Political considerations aside, it must be acknowledged that despite appearances to the contrary, the functional dynamics in operation imply that, for all intents and purposes, these Arab regional economies together with the Jewish economy constitute one macroeconomy, with a dual institutional/policy framework and structure/performance. Such a conceptual framework for analyzing Palestinian economic prospects, which recasts issues in the context of a single economy's relations to its regional components, is not a function of methodological or political preferences but of reality. Indeed, insistence on analyzing the three Palestinian regional economies in isolation from each other and from the Israeli/Jewish economy could be considered a function of outmoded nationalist ideologies. Accordingly, it is necessary to explore anew the underlying dynamics of the relationship between the Jewish and Arab economies in Israel/Palestine as constituting one macroeconomy.

For example, a simple way of viewing the imbalance in the national-regional economic relationship is to estimate the share of the Palestinian Arab regional economies in the total GNP of the macroeconomy of the Israeli-Palestinian economic union. In 2006, total Israeli GNP was \$141 billion, including some \$11 billion originating in the Arab regional economy.<sup>26</sup> When added to the

GNP of the occupied territories, this amounts to a total of \$146 billion, with the Arab regions therein accounting for \$16 billion. This is strikingly low considering that the Palestinian Arabs within the borders of Israel/Palestine constitute around 45 percent of the population living in that territory (but produce only around 11 percent of its national income). This highlights the scale of the challenge of Jewish/Arab economic convergence, which remains further away on the horizon than it was six decades ago, when Arabs constituted 70 percent of the total population of Mandate Palestine, but their share of national income was still 40 percent.<sup>27</sup>

The purpose of engaging at this late stage in a collective, interdisciplinary effort to investigate the conditions and prospects of the Arab economy in Israel should above all be to contribute to the elaboration of an "actionable" economic and social development vision and the necessary policies and mechanisms to achieve it. Such an analysis should set the stage for a development policy planning framework that could deliver sustainable social and economic gains for the Arab-Israeli economy, as one of the three less-developed regions of the Israeli-Palestinian "economic union." This is imperative for several reasons. Most immediately, this neglected sector of the Palestinian people has a unique development experience from which the other segments could learn and build upon. Of equal importance is the Arab community's geographical/political/economic position within the long struggle over the land of Palestine/Israel and the need to factor that into any lasting resolution of the Palestinian-Israeli conflict. This was most recently recognized by Palestinian president Mahmud Abbas, who, in the wake of demands that the PLO recognize the Jewish character of Israel, stated that he had rejected attempts to negate the existence of almost 1.5 million Palestinian Arabs. If nothing else, this region, currently excluded from the peace process, should benefit from any "peace dividend" that might emerge in the context of a comprehensive regional settlement and the expected development cooperation and resources that might ensue.

Whatever the ultimate reconfiguration of borders and the government that might emerge if a peace process resumes, such a policy framework should be capable primarily of *responding to Palestinian Arab development needs under any circumstances*, whether a continuation of the status quo or an implementation of the two-state or even a one-state solution. Although the future of Palestinian citizens in Israel and their compatriots in the WBGS might proceed along different political tracks, the common features of their historical relationship with the Israeli national economy are too glaring to ignore. Moreover, the similarities in their economic structure and performance are an outcome of similar processes delivering similar results in different "legal" contexts and at different stages of the conflict. Ultimately, the long-term prospects and viability of the Jewish/Israeli economy itself depend on a more sustainable and peaceful form of economic dualism, even if a cost is to be incurred in redressing regional imbalances and narrowing economic disparities.

Thus, the hypothesis that the economic union designed in 1947 for partitioned Palestine has acquired a real existence has a direct bearing on how to address Palestinian development policy for the future. If circumstances

continue to undermine the possibility of forging ahead and implementing partition (politically and territorially, with two states), then current realities should be accepted as having overridden any remaining political imperative for separate sovereignties in Palestine. This suggests the relevance of a *Palestinian Arab tri-regional development program* in the context of a future one state-solution—one that would aim to transform the Bantustan-type economic relationship that exists today into an integrated, bi-national dual economy development program. And if an independent and viable Palestinian state in the WBGs is ever to see the light of day, the new Arab regional economic paradigm outlined here can be a strategic asset for the Palestinian people, and, if treated in the spirit of 1947, maybe even for peace.

## NOTES

1. Other terms used to refer to this population (depending on the commentator's viewpoint) include "Palestinian Arabs in Israel," "Arabs of Israel," "Arabs in Israel," and "Arab minority in Israel."

2. In this paper, the economy of the Arab region in Israel is synonymous with "Arab regional economy" in Israel and "Arab-Israeli economy." Other common usages include the "Arab sector" or "Arab minority." Here "Israel/Palestine" refers to the territory of pre-1948 Mandate Palestine (i.e., present-day Israel and the West Bank/Gaza Strip).

3. The most recent comprehensive treatment of the subject may be found in J. Metzger, *The Divided Economy of Mandatory Palestine* (New York: Cambridge University Press, 1998).

4. Two contemporaneous accounts of the Mandate economy are S. Himadeh, *Economic Organisation of Palestine* (Beirut: American University of Beirut, 1939) and J.B. Hobman, *Palestine's Economic Future* (London: Lund Humphries, 1946).

5. The course of economic integration between sovereign nations (as for example followed in postwar Europe) usually goes from preferential to free-trade to customs union (as with the European Economic Community) to monetary/currency union (as with the European Monetary Union) to full economic union (still unattained in Europe).

6. Similar to UNGA Res. 181, the Oslo accords included "Annex on Economic Relations" (known as the Paris Protocol), which enshrined and codified a modified version of the customs union between

Israel and the occupied territories that was in force since 1967.

7. This figure excludes Palestinians living in East Jerusalem, which Israeli statistics include as "Arab-Israelis." The Arabs in Israel also constitute one-fifth of the Palestinian Arab population living within historic Palestine.

8. See Special Document file in *Journal of Palestine Studies* 36, no. 4 (Summer 2007), 73–103.

9. Y. Ben Porath, *The Arab Labor Force in Israel* (Jerusalem: Maurice Falk Institute, 1966); S. Zarhi and A. Achziera, *The Economic Conditions of the Arab Minority in Israel* (Tel Aviv: Center for Afro-Asian Studies, 1966); F. Gottheil, "On the Economic Development of the Arab Region in Israel" in M. Curtis and M. Chertoff, eds., *Israel, Social Structure and Change* (New Brunswick, NJ: Transaction Books, 1973); M. Arnon and M. Raviv, *From Fellah to Farmer: A Study on Change in Arab Villages* (Rehovot, Israel: Study Settlement Center, 1980); E. Yalan et al., *The Modernization of Traditional Agricultural Villages: Minority Villages in Israel* (Rehovot, Israel: Study Settlement Center, 1972); Y. Bar-Gal, *Geographical Changes in the Traditional Arab Villages in Israel* (Durham, UK: Center for Middle East and Islamic Studies, 1980); D. Czamanski and M. Meyer-Brodnitz, "Industrialisation in Arab Villages in Israel" in R. Bar-El, ed., *Industrialization in Rural Israel* (Boulder, CO: Westview Press, 1986); M. Semyonov and N. Lewin-Epstein, *The Arab Minority in Israel's Economy: Patterns of Ethnic Inequality* (Boulder, CO: Westview Press, 1993).



10. Ruth Klinov, Ephraim Kleiman, and Meirav Yftach, "Market integration and separation of the Arab and Jewish sectors in Israel" (unpublished paper, 2004).

11. B. Abu Kishk, "Arab Land and Israeli Policy," *Journal of Palestine Studies* 11, no. 1 (Fall 1981), pp. 124-35; H. Rosenfeld, "The Arab Village Proletariat," *New Outlook* 7, no. 3 (1962); H. Rosenfeld, "The Class Situation of the Arab National Minority in Israel," *Comparative Studies in Society and History*, no. 20 (July 1978); N. Makhoul, "Employment Structure of the Arabs in Israel," *JPS* 11, no. 3 (Spring 1982), pp. 77-102; E. Zureik, *Palestinians in Israel: A Study in Internal Colonialism* (London: Routledge and Kegan Paul, 1979); I. Lustick, *Arabs in the Jewish State: Israel's Control of a National Minority* (Austin: University of Texas Press, 1980); M. Sofer, I. Schnell, and I. Drori, "Industrial Zones and Arab Industrialisation in Israel," *Human Organization* 55, no. 4 (Winter 1996); A. Haidar, *On the Margins: The Arab Population in the Israeli Economy* (New York: St. Martin's Press, 1995); R. Khamaisi, *Planning and Housing Among the Arabs of Israel* (Tel Aviv: International Center for Peace in the Middle East, 1990); R. Khalidi, *The Arab Economy in Israel: Dynamics of a Region's Development* (London: Croom Helm, 1988).

12. This relationship was most recently analyzed in the context of a mercantilist relation in A. Shehadeh, *De-development: Israeli Economic Policies toward the Arab National Minority* [in Arabic], (Haifa: Mada al-Carmel Center, 2006). Another recent contribution to an indigenous socioeconomic narrative is provided in The Galilee Society, *Palestinians in Israel, 2004: Socioeconomic Survey* (Shafamr: The Galilee Society and Mada al-Carmel Center, 2005). This latter publication was not the first of its kind: In 1992, the now-defunct Jaffa Research Center (Nazareth) published the first indigenous statistical field survey findings on Arab cities and villages in Israel.

13. This process is similar to that of "de-development" analyzed by Sara Roy and to the concept of "adverse path-dependence" introduced by UNCTAD in research on the Palestinian economy in the occupied territories.

14. Raja Khalidi, *The Arab Economy in Israel: Dynamics of a Region's*

*Development* (London: Croom Helm, 1988). See also R. Khalidi, "The Arab Economy in Israel: Dependency or Development," in *JPS* 13, no. 3 (Spring 1984), pp. 63-86.

15. This had become a rallying slogan of the Palestinian nationalist revival in Israel during the 1980s and until the signing of the Oslo Accord.

16. ICBS, *Characterization and Classification of Local Authorities by the Socioeconomic Level of the Population, 2003*.

17. Those not covered comprise Israeli kibbutzim and the smallest Arab villages, plus about forty Arab villages and localities (mainly settled Bedouin) not recognized by the state.

18. All of the following gaps would be sharper if comparisons were made between all Arab localities with all Jewish localities rather than with the national averages.

19. ICBS, *Statistical Abstract of Israel 2005*.

20. 1 dunam = 1000 square meters, or one-fourth of an acre.

21. *Statistical Abstract of Israel 2005*, Table 19.6.

22. *Participation rate* measures the proportion of the working age population actually employed or seeking employment. Labor force data presented here are for 2000 and are taken from ICBS, *Statistical Abstract of Israel 2005*, Table 12.20.

23. The Palestinian economy and the policy environment shaping it has spawned voluminous literature over the decades, including reports and studies by United Nations and international agencies too numerous to reference here.

24. In the classic dependency model, the relation between the dominant and dominated economies is that of a hub-to-spoke link, whereby the functional economic relation is between the center and the periphery, with limited exchange between the peripheries themselves.

25. Some observers would argue that PA autonomy was illusory and never really existed.

26. According to the Center for Development of Arab and Jewish Enterprise, quoted in *Ha'Aretz*, 10 September 2007.

27. E. Zureik, *The Palestinians in Israel*, p. 58.